Investors Should Approach Cryptocurrency with Caution, Delaware's Investor Protection Unit Says

With cryptocurrencies attracting recent headlines, the Investor Protection Unit of the Delaware Department of Justice is urging Delaware investors to be cautious about investments involving cryptocurrencies.

"Investors should make certain they understand the risks associated with investments in cryptocurrencies and financial products involving cryptocurrency before they invest," said Director of Investor Protection Greg Strong.

Cryptocurrencies are a medium of exchange that are created and stored electronically in the blockchain, a distributed public database that keeps a permanent record of digital transactions. Current common cryptocurrencies include Bitcoin, Ethereum and Litecoin. Unlike traditional currency, these alternatives have no physical form and typically are not backed by tangible assets. They are not insured or controlled by a central bank or other governmental authority, cannot always be exchanged for other commodities, and are subject to little or no regulation.

A survey of state and provincial securities regulators by the North American Securities Administrators Association (NASAA), of which the Investor Protection Unit is a member, shows 94 percent believe there is a "high risk of fraud" involving cryptocurrencies. Regulators also were unanimous in their view that more regulation is needed for cryptocurrency to provide greater investor protection.

"The rapid price swings in cryptocurrency-related investments may tempt investors to invest in cryptocurrency without first becoming knowledgeable about the risks involved," Greg Strong said. "Cryptocurrencies and investments tied to them are extremely volatile and highly speculative investments. Combined with a high risk of fraud, cryptocurrencies are high-risk investments."

Last month, NASAA identified Initial Coin Offerings (ICOs) and cryptocurrency-related investment products as emerging investor threats for 2018. Unlike an Initial Public Offering (IPO) when a company sells stocks in order to raise capital, an ICO sells "tokens" in order to fund a project, usually related to the blockchain. The token likely has no value at the time of purchase. Some tokens constitute, or may be exchangeable for, a new cryptocurrency to be launched by the project, while others entitle investors to a discount, or early rights to a product or service proposed to be offered by the project.

NASAA offers a short animated video to help investors understand the risks associated with ICOs and cryptocurrencies. NASAA and its members first alerted investors of the risks associated with cryptocurrencies in 2014.

Common Cryptocurrency Concerns

Some common concerns investors should consider before investing in any offering containing cryptocurrency include:

- Cryptocurrency is subject to minimal regulatory oversight, susceptible to cybersecurity breaches or hacks, and there may be no recourse should the cryptocurrency disappear.
- Cryptocurrency accounts are not insured by the Federal Deposit Insurance Corporation (FDIC), which insures bank deposits up to $250,000.
- The high volatility of cryptocurrency investments makes

them unsuitable for most investors, especially those investing for long-term goals or retirement.

- Investors in cryptocurrency are highly reliant upon unregulated companies, including some that may lack appropriate internal controls and may be more susceptible to fraud and theft than regulated financial institutions.
- Investors will have to rely upon the strength of their own computer security systems, as well as security systems provided by third parties, to protect purchased cryptocurrencies from theft.

Common Red Flags of Fraud

The Investor Protection Unit also reminds investors to keep watch for these common red flags of investment fraud:

- **"Guaranteed" high investment returns.** There is no such thing as guaranteed investment returns, and there is no guarantee that the cryptocurrency will increase in value. Be wary of anyone who promises a high rate of return with little or no risk.
- **Unsolicited offers.** An unsolicited sales pitch may be part of a fraudulent investment scheme. Cryptocurrency investment opportunities are promoted aggressively through social media. Be very wary of an unsolicited communication—meaning you didn't ask for it and don't know the sender—about an investment opportunity.
- **Sounds too good to be true.** If the project sounds too good to be true, it probably is. Watch out for exaggerated claims about the project's future success.
- **Pressure to buy immediately.** Take time to research an investment opportunity before handing over your money. Watch out for pressure to act fast or "get in on the ground floor" of a new tech trend.
- **Unlicensed sellers.** Many fraudulent investment schemes involve unlicensed individuals or unregistered firms. The Investor Protection Unit of the Delaware Department

of Justice can help investors research the background of those selling or advising the purchase of an investment. The Investor Protection Unit can be reached at 302-577-8424 or through our website at https://attorneygeneral.delaware.gov/fraud/ipu/.